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IN THE

SUPREME COURT OF THE UNITED STATES.

Filed Dec. 19, 1899.

OCTOBER TERM, 1899.

No. 429.

FRED BARDES, Trustee of the Estate of Frank T. Walker, Bankrupt, *Complainant*,

vs.

FIRST NATIONAL BANK OF HAWARDEN, Iowa, THE BANK OF ALCESTER, of Alcester, South Dakota, and CHARLES R. ALLEN, *Defendants*.

On Questions Certified from the District Court of the United States for the Northern District of Iowa.

JOHN HUTCHINSON, Hawarden, Iowa,
WILLIAM MILCHRIST, Sioux City, Iowa,
Solicitors and of Counsel for Defendant, First National Bank of Hawarden, Iowa.

DEFENDANT'S BRIEF.

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DEFENDANT'S BRIEF.

Complainant, as trustee of Frank T. Walker, bankrupt, brought this action to recover from the defendants the value of certain property, alleged to have been conveyed to them by the said Walker, within four months of his being adjudged a bankrupt. The complainant and defendants are shown to be residents of the state of Iowa. Defendants demurred upon the ground

that the court was without jurisdiction, for the reason that the controversy was between citizens of the same state. The district court, desiring the opinion of the supreme court, certified four questions set forth in the record and in the brief of counsel for complainant.

The first clause of *section 23*, of the Bankrupt Act, provides that the "United States circuit courts shall have jurisdiction of all controversies at law and in equity, as distinguished from proceedings in bankruptcy between trustees as such and adverse claimants, concerning the property acquired or claimed by the trustee in the same manner and to the same extent only as though bankruptcy proceedings had not been instituted, and said controversy had been between the bankrupts and such adverse claimants." The jurisdiction here conferred includes all proceedings as distinguished from proceedings in bankruptcy, involving the requisite amount and between proper parties.

If the contention of counsel for complainant that the district courts, as courts of bankruptcy, have jurisdiction regardless of the amount involved or the citizenship of the litigants, is correct, then the first clause of said *section 23* is of no material force or effect. If the district courts have jurisdiction without regard to the amount involved or the citizenship of the parties, why confer jurisdiction on the circuit courts in the limited manner defined in said *section 23?*

The second clause of said *section 23* further limits the jurisdiction of the United States courts, by providing that "suits by the trustee shall only be brought or prosecuted in the courts where the bankrupt, whose estate is being administered by such trustee, might have brought or prosecuted them, if proceedings in bankruptcy had not been instituted, unless by consent of the proposed defendant." Said *section 23* refers to all controversies of law and equity distinguished from proceedings in bankruptcy, apparently leaving the jurisdiction of the district courts exclu-

sively in proceedings in bankruptcy. It is, therefore, material to determine if the case at bar is a "proceedings in bankruptcy," within the meaning of the act.

As to what constitutes proceedings in bankruptcy was determined in the case of *Kidder vs. Horrobin et al.*, 72 N. Y., 164. In the opinion it is said, "By section one of the Bankrupt Act, as originally enacted March 2, 1867, the district courts of the United States were constituted courts of bankruptcy, with original jurisdiction in their respective districts in all matters and proceedings in bankruptcy, and with authority to hear and adjudicate upon the same according to the provisions of the act. The section declares that the jurisdiction shall extend to certain enumerated cases; among others, 'to the collection of all the assets of the bankrupt.' In construing this section it has been held that as jurisdiction in bankruptcy was statutory, it was necessarily exclusive in the courts which were designated as courts of bankruptcy, and vested with jurisdiction in bankrupt proceedings by the Bankrupt Act. But it was also held that the declaration, in the same section, that the jurisdiction of the district courts should extend to the collection of the assets of the bankrupt, did not exclude the jurisdiction of the state courts in actions by the assignee to recover the assets of the bankrupt. The same construction was given to similar provision in the Bankrupt Act of 1841. (*Ex parte Christy*, 3 How. (U. S.) 319; *Nugent vs. Boyd, id.*, 426; *Ward vs Jenkins*, 10 Metc., 583.)

"The first section of the Bankrupt Act was amended by the act of congress, approved June 22, 1874, by adding thereto this proviso: 'Provided that the court having charge of the estate of any bankrupt may direct that any of the legal assets or debts of the bankrupt as contradistinguished from equitable demands, shall, when such debt does not exceed $500, be collected in the courts of the state where such bankrupt resides, having jurisdiction of the claims of such nature and amount.' It is claimed

that this proviso is to be construed as conferring upon the state courts jurisdiction of actions for the collection of the debts and assets of the bankrupt, directed by the bankrupt court to be brought in the state courts, and by implication to exclude jurisdiction in all other cases. We, however, concur in the view expressed by the supreme court of Massachusetts in *Goodrich vs. Wilson* (119 Mass , 429), that the effect of this amendment is not to confer or take away jurisdiction of the state court, but simply to allow the federal courts to decline to entertain actions at common law, to which the assignee is a party, in which the debt demanded is less than the amount which determines the jurisdiction of these courts in other cases.

"It is also claimed that the state courts are deprived of jurisdiction of actions by assignees in bankruptcy, to recover debts due to the bankrupt, by section 711 of the revised statutes of the United States, which declares that the jurisdiction vested in the courts of the United States in the cases and proceedings mentioned in the section shall be *exclusive* of the courts of the several states. This declaration is followed by a specification of eight classes of cases, of which the sixth is 'of all matters and proceedings in bankruptcy.' The argument is that a suit brought by an assignee in bankruptcy to collect a debt due to the bankrupt is a matter and proceeding in bankruptcy, and that the jurisdiction of the state courts is therefore excluded. We do not think that a suit brought for this purpose is a matter or proceedings in bankruptcy within the meaning of section 711 * * * * * It may be difficult to make a complete definition of what are matters and proceedings in bankruptcy within section 711, but it may be stated in general terms that they are the matters and proceedings which pertain to the special and peculiar jurisdiction of the federal courts as courts of bankruptcy. The adjudication of the bankruptcy; the appointment of assignees and other agents for the administration of the system; the vesting of the title to the bankrupt's prop-

erty in the assignee; the marshaling and distribution of the assets; the discharge of the bankrupt from his debts; these and other like powers belong to the jurisdiction in bankruptcy, and are matters and proceedings in bankruptcy of which state courts have no jurisdiction. But when a common law action is an appropriate remedy to enforce a right asserted by the bankrupt act, or existed in favor of the bankrupt before the bankruptcy, an action to enforce or vindicate the right is not a matter or proceeding in bankruptcy within section 711. The exercise of the original and ordinary jurisdiction of the state courts in such cases is in no proper sense an exercise of jurisdiction in bankruptcy. The fact that the plaintiff makes his title under the Bankrupt Act by assignment from the debtor, or by force or operation of the act itself, does not make the suit a matter or proceeding in bankruptcy, any more than would a suit brought by an assignee appointed under the state insolvent law, to recover a debt owing to the insolvent, be a proceeding or matter in insolvency. It is quite clear that the state courts are not deprived of jurisdiction of actions, by assignees, to collect the assets of the bankrupt by the section referred to. If this was the intention of congress, it is reasonable to suppose that it would have been explicitly declared, and an intention to deprive state courts of jurisdiction will not be inferred from doubtful language, nor will the words of a statute be extended beyond their strict meaning to accomplish this result."

Section 2 of the act defines the jurisdiction of courts of bankruptcy, and said courts are required by clause 7 of said section, to "cause the estate of bankrupts to be collected, reduced to money and distributed, and determine controversies in relation thereto, except as herein otherwise provided." *Section 23* is evidently the exception referred to in said clause. The estate referred to in said clause 7 evidently refers to the property in possession of the trustee and within the actual jurisdiction of the district court. As to such property claimants might have to as-

sert their right thereto in the bankrupt, or district court, as the jurisdiction of said court probably would be exclusive. In the case at bar the title to the property in controversy is in the defendants, and the trustee can only defeat the title and ownership of defendants by an adjudication in a court of competent jurisdiction that the property was fraudulently transferred.

The right to appoint arbitrators under *section 26* of the act must be limited to controversies arising in the district court. If any other court has jurisdiction to determine controversies between the trustee and claimants of property, such court would not submit to have its jurisdiction interfered with, or be practically deprived of jurisdiction by the action of the district court in appointing arbitrators to determine the rights of the parties as to the controversies pending in said court.

To support the jurisdiction of the district court, counsel for complainant have cited a few cases from the district courts.

In *Re Severs*, 91 Fed. Rep., 367, the only question presented was that of the right of creditors to apply for the appointment of a receiver to take charge of assets in the hands of the assignee of the party declared to be a bankrupt, before the appointment of a trustee. It is held that such right existed, and that as the making of a general assignment for the benefit of creditors is of itself an act of bankruptcy, the assignment law, under which the assignment was made, was suspended, and the assignee acquired no right, title or interest in and to the property assigned. This decision was affirmed upon appeal, in the case of *Davis vs. Boehle*, 92 Fed. Rep., 325.

In Re Brooks, 91 Fed. Rep., 508, is next cited by complainant's counsel. That was an action brought by the trustee to secure the return of property sold under the foreclosure of a chattel mortgage executed by the bankrupt, after the mortgagor had been adjudged bankrupt, but before the appointment of a trustee. In the decision it is said "the mortgagor has a right to re-

deem, which continues all the way to the time of sale (Sec. 2264), of which he and those claiming under him are entitled to notice (Sec. 2266). After the filing of the petition there was no one to act upon a notice, or upon whom notice could probably be given, until there should be a trustee, and the petitioner could not lawfully proceed according to the provisions of the statute of the state, nor without the leave of the court having the jurisdiction and control of the property. The taking away of the property is not only an unlawful interference with the jurisdiction of the court, but the receiving of 'any material amount of property from a bankrupt after the filing of the petition, with intent to defeat this act' is made highly penal. (Sec. 29 B.) That an officer having exclusive possession of the property of a bankrupt could not lawfully proceed, after bankruptcy proceedings, without notice, was treated as unquestionable in the case of *Connor vs. Long*, 104 U. S., 228."

This case does not apply, as in the case at bar; the property in controversy had been sold and transferred before the petition was filed, asking that Walker be adjudged a bankrupt.

The case of *Carter vs. Hobbs et al.*, 92 Fed., 594, is also cited by counsel for complainant. Said action was brought to set aside as fraudulent a mortgage executed by the bankrupt within four months of the filing of a petition for his adjudication as a bankrupt. In the decision rendered it is said, on *page 597*, "It is next insisted that this Court is without jurisdiction, and that the bankrupt's estate, which has passed under the custody of the court, and is now in the possession of its trustee, can only be cleared of the fraudulent encumbrances placed thereon by a suit brought in the court of the state. The trustee is vested by operation of law with the title of the bankrupt as of the date of the adjudication, among other things, to all property transferred by him in fraud of his creditors, as well as to all property which, prior to the filing of the petition, he could, by any other means,

have transferred, or which might have been levied upon and sold by judicial process against him. *Bankruptcy Act, Sec. 70.* The word "transfer" includes the sale and every other different mode of disposing of or parting with property, or the possession of property, absolutely or conditionally, as by payment, pledge, mortgage, gift or security. *Id. Sec. 1, cl. 25.* Therefore, the title to the bankrupt's property, encumbered by the mortgages and lease, was transferred by operation of law to, and vested in, the trustee, an officer of this court. The decree operates in *rem*, and from the moment of the adjudication of bankruptcy the bankrupt's estate is in *custodia legis*, and under the jurisdiction of this court. It is fundamental that no court or individual can interfere with such custody or possession. The assertion of any right against, or to participate in the *res so* in *custodia legis* must be sought in the court in whose custody it is. An attempt to assert such right elsewhere would be rewarded as a contempt. The adjudication proceeds in *rem*, and all persons interested in the *res* are regarded as parties to the bankruptcy proceedings. These parties include not only the bankrupt and trustee, but also all the creditors of the bankrupt."

In the above case the court acquired full control and jurisdiction over the mortgaged property, and should have the right to determine all controversies in relation thereto. An entirely different case would have been presented had there been a sale of the property so that the right of the bankrupt and his title thereto could only be established after it had been determined that the sale was fraudulent within the meaning of the Bankrupt Act.

In *Re Gutwillig*, 90 Fed. Rep., 481, it was held that the court of bankruptcy had jurisdiction to enjoin the disposition of the property by the assignee of the bankrupt, pending the hearing of the petition of the bankrupt, and this decision was affirmed with the court of appeals, *92 Fed., 337.*

The foregoing were cases cited by counsel, and in none of them is it held that the discrict court has jurisdiction to determine controversies between the trustee and the claimant of property transferred and sold, prior to the adjudication in bankruptcy. The right to bring such an action is fully considered in *In Re Abraham*, 98 Fed., 767, where the court, after reviewing the various provisions, says: "The general rule is, a person can be sued in the United States court only in the district whereof he is an inhabitant, and no such action can be brought in those courts unless the matter in dispute exceeds, exclusive of interest and cost, the sum or value of $2,000. It is therefore apparent, that, as a general rule, all controversies at law and in equity as distinguished from proceedings in bankruptcy between trustees, as such (or other duly appointed, empowered representatives of the bankrupt's estate), and adverse claimants, concerning the property acquired or claimed by the trustee (or other duly appointed and empowered representative of the state), which cannot, or are not adjusted by negotiation, arbitration or compromise, must be abandoned by the trustee or adjudicated in the state courts, unless by consent of the proposed defendant suit can be brought in a United States court."

The above case expressly decides that the district court has no jurisdiction of an action between the trustee and a third party, involving the validity of a sale made of property by the bankrupt, prior to the adjudication in bankruptcy, and said case is in harmony with the case of *Mitchell vs. McClure*, 91 Fed., 621.

In the case of *Burneet vs. Morris Mercantile Co.*, 91 Fed., 365, section 23 of the Bankrupt Act is cited, and in relation thereto it is said: "It is clear that congress intended that the jurisdiction to set aside conveyances as made in fraud of creditors should not be enlarged by any operation of the Bankrupt Act; that the jurisdiction in these cases should be determined with reference to the law as it then was. Any construction in favor of the jurisdiction

of the district court of the United States based upon provisions of the law of general application is in conflict with the section quoted. It is argued that because the bankrupt cannot maintain a suit to set aside a conveyance as fraudulent, made by himself, therefore the provision quoted does not apply in a case like this. But this is a question of jurisdiction—a question of the right to determine, not of the principles to obtain in reaching a determination. If the bankrupt himself brought the suit he could not be turned out of court on the question of jurisdiction. The authority of the court to decide as to his rights would be unquestioned, although he might be precluded in his right to relief by his own act. The statute intends to keep all controversies as to the validity of conveyances like these where they would have been if the Bankrupt Act had not been passed. The question of the validity of these conveyances is the vital question. That question, in the absence of the Bankruptcy Act, must necessarily be determined in any proceedings brought, therefore, by the courts of the state, unless the case involves the requisite amount to give a federal court jurisdiction, and is between citizens of different states."

The jurisdiction of the district court involving the title to property is again decided in the case of *Hicks vs. Knost*, 94 Fed., 627, where the court holds that the limitation of jurisdiction referred to by the exception in clause 7 of section 2 is found in section 23, and in referring to said sections the court says: "It is said in support of these rulings that a construction of the exception in clause 7 of section 2, which would remit to the courts of the state jurisdiction over all suits for the collection of debts and demands due the bankrupt, would be repugnant to the body of the act, and not admissible. Is this true? Whether it is or not must be determined from an examination of the act itself, with a view to ascertain its general purpose and intent. The object and purpose of the law is (1) to discharge honest bankrupts from their debts, and (2) to secure to their creditors

an equal distribution of their estates. Now, is it necessary, within the meaning of the law, in order to accomplish these ends, to invest bankruptcy courts with jurisdiction to hear and determine all controversies incident to the collection and conversion into money of the bankrupt's estate? Must all suits and actions for that purpose, actions on accounts, promissory notes, and contracts, and suits to forclose mortgages, set aside fraudulent conveyances, and the like, be brought in the bankruptcy courts, without reference to the amount involved, the citizenship of the parties, or the questions presented? Must the dockets be crowded, and the time of the district courts be taken up with the hearing of minor controversies, at great inconvenience and expense to the litigants, who may be compelled to travel long distances to attend the courts, or was it the intention of congress to follow its long-established policy of permitting such controversies to be determined in the local state courts, at the doors of the people, without unnecessary expense or inconvenience? It is the policy of congress to require all controversies, where the amount involved is less than $2,000, to be determined in the state courts, notwithstanding they may involve a federal question or the parties be of diverse citizenship, and the construction of the Bankrupt Act, insisted upon by the complainant, would antagonize and defeat that policy, in so far as controversies arising under that act are concerned. The consistent adherence of congress to this policy is illustrated by the act of August 13, 1888 (25 Stat., 433), permitting receivers appointed by United States courts to be sued in the state courts, and, if congress intended by the Bankrupt Act to establish an exception repugnant to this general policy, it should clearly appear from the language of the law, without the aid of ingenious construction."

This question is again presented in the following cases:

Goodyear vs. Barnes et al., 94 Fed., 798.
Camp vs. Zellars, 94 Fed., 799.
In Re Oggles, 93 Fed., 426.
In Re Rice et al., 92 Fed., 987.

Section 25 of the Bankruptcy Act defines the cases in which appeals may be taken, but does not provide for the right of appeal in actions between the trustee and a third person. It is fair to assume that if such litigation in the district court had been contemplated the right to appeal would have been provided for.

The decision under the former Acts of Bankruptcy are conflicting, and it is not deemed that any material aid can be derived from their consideration in the construction of the present Bankrupt Act.

Respectfully submitted,

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